ALTMAN INVESTMENT MANAGEMENT

FIXED INCOME STRATEGY HIGHLIGHTS — MAY, 2023

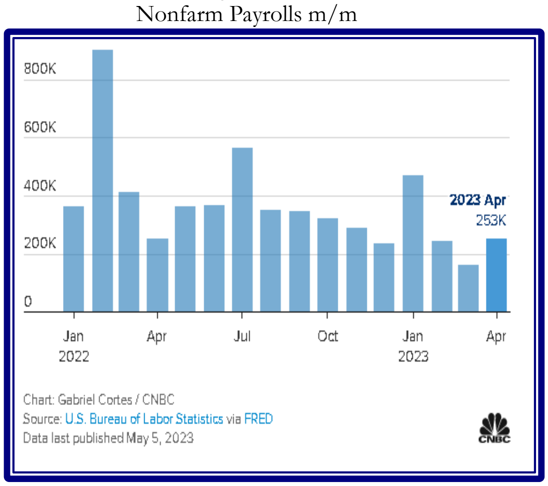
IN BRIEF: The U.S. Fixed Income Markets, Performance, and Strategy

The Fed once again lifted its key interest rate by 25 basis points in early May to a level of 5-5.25%. This was expected based upon relevant macroeconomic data that underscores cooling inflationary pressures, normalizing economic growth and a tight labor market. In his remarks, Fed Chairman Powell dropped the language that it anticipates that additional policy firming would be necessary. He also noted uncertainty surrounding the impact of banking stresses on credit conditions. Between now and the next meeting in June, the Fed intends to monitor the impact of the monetary steps taken so far, alongside evolving credit conditions and employment trends.

The April jobs report was stronger than expected citing an increase of 253,000 in nonfarm payrolls, following 3 months of consecutive declines in job creation. Unemployment came in at 3.4% - one of the lowest levels in decades. Average hourly earnings clocked in at 0.5% month over month. This report, during a time of rising calls for a recession, layoff announcements and banking turmoil, provides some support for markets and should temper volatility. The Fed will be watching the pace of job growth and the extent of rising employment earnings in its determination for the direction of rates at its next meeting.

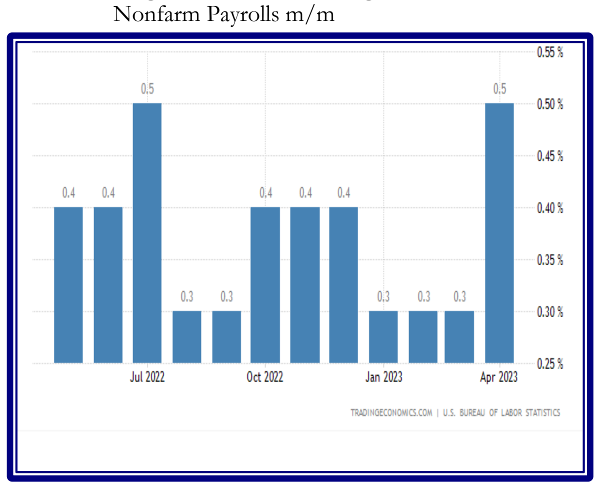
Monthly Job Growth

Nonfarm Payrolls m/m



Average Hourly Earnings

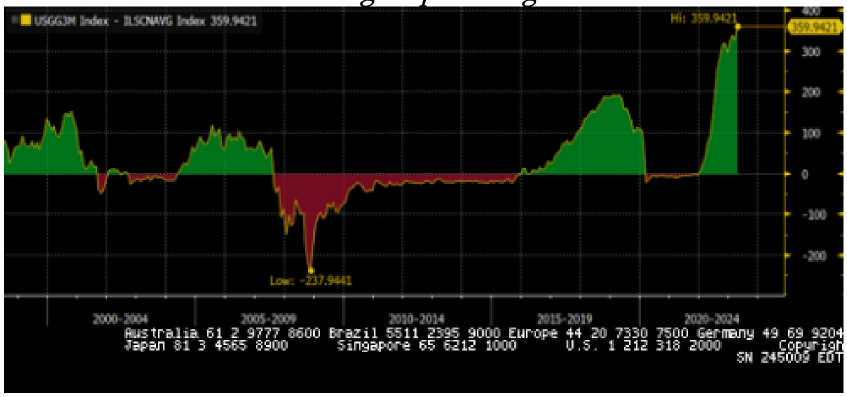
Nonfarm Payrolls m/m



Sources for both charts: U.S. Bureau of Labor Statistics

The case for lower rates hinges on evolving credit conditions. According to Bank of America Global Research (BofA), quantitative tightening worked against mortgage-backed securities, a major asset holding by banks. On top of this, rising interest rates relative to 0% deposit rates increases competition for deposits for savers seeking to keep pace with inflation. Declining assets at banks spilled over into concern for deposits igniting outflows, and in some of the more significant cases led to bank failures. BofA highlights that the yield gap between 3-month CD rates and 3-month Treasury bills is contributing to deposit flight risk (illustrated by following chart).

Yield Gap Between 3m CDs and Treasuries
is Stimulating Deposit Flight Risk



Source: Bloomberg

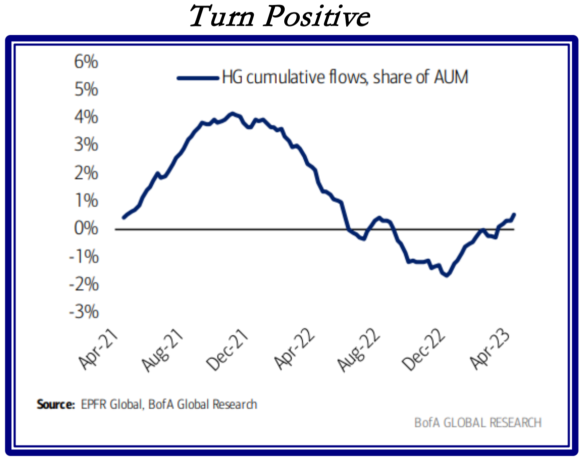
The extent and duration of the recent stress on the banking sector is indeed a consideration in Fed policy in conjunction with inflation and the labor market. We think it is less likely that credit tightening from banking stresses will be extreme enough to warrant a pivot towards easing in coming months. On the other hand, a rate hike at its next meeting would require banking stresses to subside, continued labor market tightness, and elevated inflation. We think we are in for a soft economic landing with heightened inflation giving Fed reason to pause in its policy to assess the impact of its cumulative rates hikes taken to date.

Q1 Sector Spotlight and Strategy:

➢ U.S. Treasuries

Inflows into high grade bond funds and ETFs are on the rise outpacing inflows into international, emerging markets, and U.S. equities combined. Treasuries alone saw $38 billion in inflows during the first quarter and $144 for the past 12 months, according to Fidelity Investments. The momentum towards government bond funds reflects stresses on the banking sector, uncertainty surrounding the debt ceiling and growing anticipation of market volatility.

High Grade Fund Flows
Turn Positive



The inverted yield curve over an extended period of time may be signaling a recession that in our prediction will likely be soft in nature, if at all. At 4%+ yields are most attractive less than 2 years in maturity. This is quite a large increase after trading below 1% throughout the pandemic. Uncertainty surrounding the efficacy of Fed policy, the direction of the economy, inflation etc., no one truly knows where rates will be in a year or two's time, and thus some reinvestment risk should be expected.

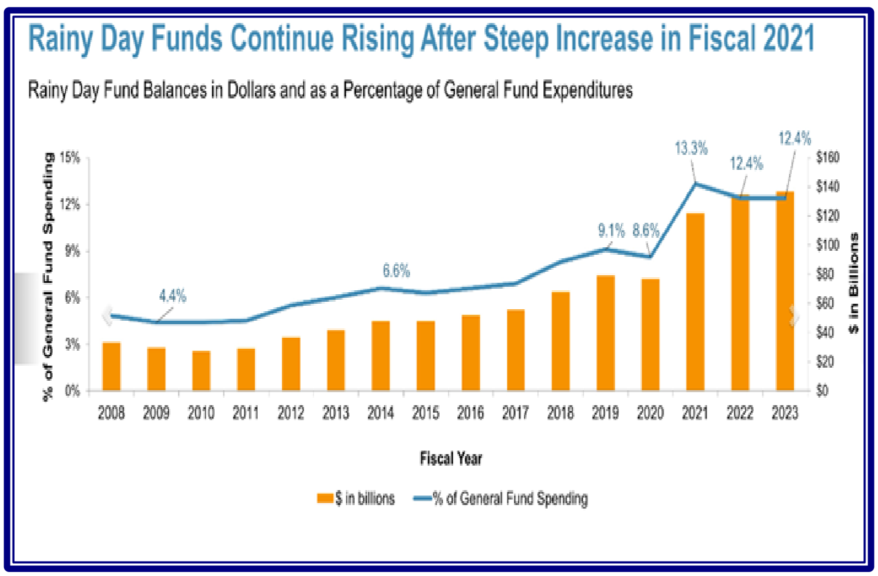
➢ Corporate Credit Markets

Corporate issuance is down 31% from a year earlier, as funding costs rise with interest rates. April is seasonally a heavier issuance month and therefore recent backlogs create the potential for increased volumes in May. Supply may also open up in order to secure lending ahead of volatility - or what credit analysts refer to as supply indigestion.

Despite slowing earnings growth, comparisons over 2022 levels are easy and remain 30% above pre-Covid levels according to Bank of America Global Research. So far, earnings have exceeded expectations by over 6% with revenue surprises of ~2%. Investment grade corporate spreads remain moderately above their historical average, offering a nice pick up in yield over U.S. Treasuries in the investment grade sectors.

➢ Municipals

Municipals had a strong Q1 in part to being on strong fiscal footing and in low supply. According to the National Association of State Budget Officers (NASBO), growth in state budgets and reserves remain strong. 2023 budgeted spending continues to grow after record breaking levels in 2022. States overall cited minimal usage of budgetary management tools generally employed in economic downturns, with only a small percentage reporting the need to target spending cuts in 2023. Rainy day funds reached new highs in 2022, providing a nice cushion. Large surpluses provide funding opportunities for states to retire a portion of their debt, supplement pensions, undergo capital construction and economic development.



Source: National Association of State Budget Offices

Revenues are expected to continue to grow in 2023, but at a slower pace after rapid growth out of the pandemic. The decline is mostly due to timing of fiscal collections in 2023 over 2022. Additionally, more than half the states are indicating collections are running ahead of original forecasts. The quality of fiscal position was evident in municipal performance during the last year, with a yield standard deviation of 1.11x vs 1.49 for U.S. Treasuries.

Healthy demand for municipals against declining new issuance supply as municipal projects are being pushed back on higher financing costs, is driving performance in the sector. With credit upgrades exceeding downgrades, there seems to be ample support for municipals going forward.

FINAL COMMENTS:

Our call for a soft landing is consistent with support from consumer spending, improving labor market and moderating inflation. Any volatility in the bond market reflecting stresses on the banking sector, uncertainty surrounding the debt ceiling, and bond supplies will likely be short lived. Our preference for higher quality corporates and municipals is no longer at the expense of owning Treasuries now that government issued yields have climbed off July lows.

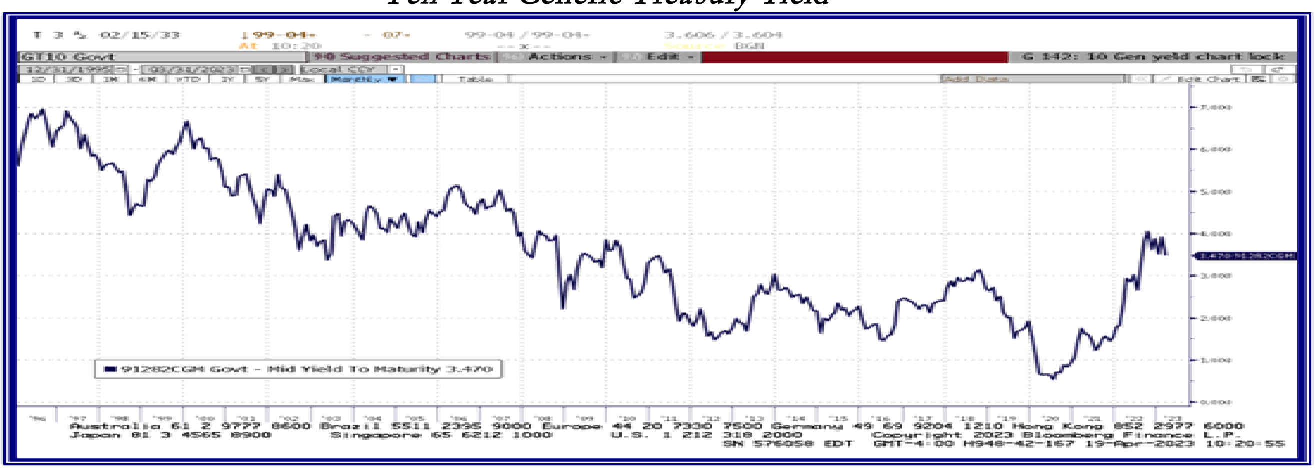
APPENDIX:

Fixed Income Sector Performance
YTD as of March 2023

	Rating	Maturity	Duration Mod Adj	Yield	Spread	Price	Trailing 12m TR
Treasury (Intermediate)	Aaa/AAA	3.97	3.69	3.87%	N/A	$93.81	-1.58%
Agency	Aaa/AA+	3.27	2.93	4.24%	0.37%	$96.86	-1.46%
MBS	Aaa/AAA	7.85	6.01	4.47%	0.60%	$89.77	-4.52%
Municipal	AA2	4.64	3.28	2.68%	-1.19%	$105.86	1.62%
Corporate (Intermediate)	AA2	5.79	5.17	4.32%	0.45%	$93.41	-2.06%
High Yield	B1	5.27	4.03	8.43%	4.56%	$88.00	-3.56%

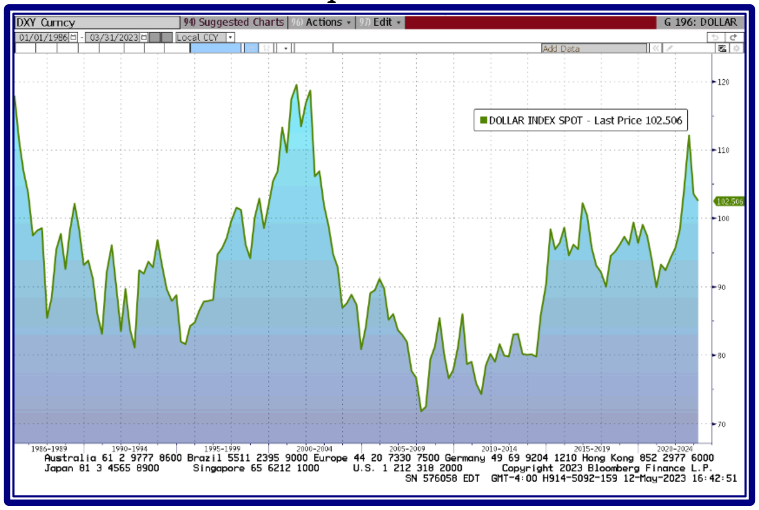
Source: Bloomberg and Altman Investment Management, LLC

Ten Year Generic Treasury Yield



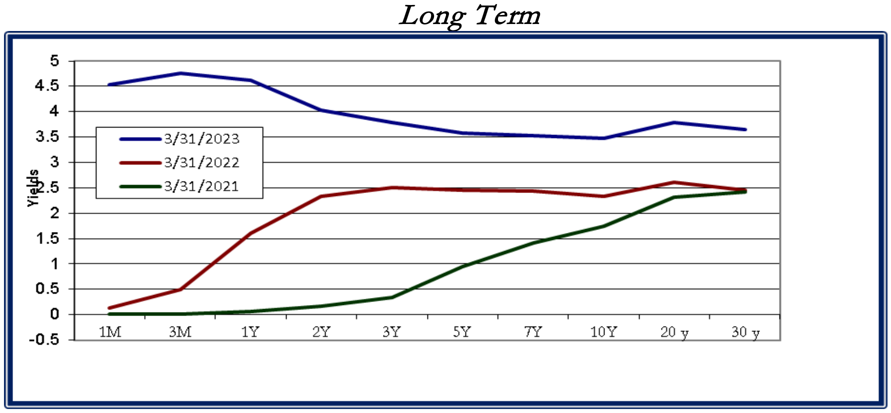
Source: Bloomberg and Altman Investment Management, LLC

Dollar Spot Index Price



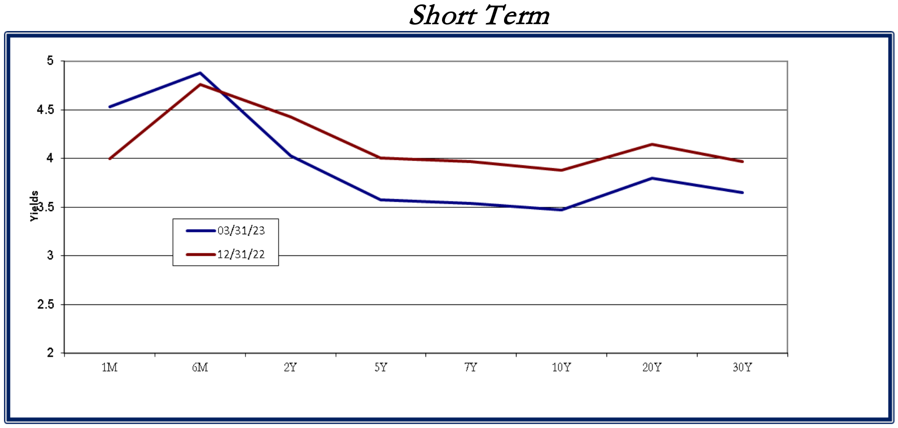
Source: Bloomberg and Altman Investment Management, LLC

Active Government Yield Curve
Long Term



Source: Bloomberg and Altman Investment Management, LLC

Active Government Yield Curve
Short Term



Source: Bloomberg and Altman Investment Management, LLC